

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF:

APPLICATION OF KENTUCKY)	
UTILITIES COMPANY FOR AN ORDER)	
APPROVING CERTAIN ACCOUNTING)	CASE NO. 10214
TREATMENT OF AMOUNTS PAID FOR)	
COAL CONTRACT RELEASE)	

INTERIM ORDER

On April 6, 1988, Kentucky Utilities Company ("KU") filed an application with the Public Service Commission ("Commission") seeking approval of its proposed method of accounting for a \$14.5 million lump sum payment to Coal Ridge Fuel, Inc. ("Coal Ridge"), as consideration for release from a 1983 coal supply agreement. KU proposed to amortize and recover the prepayment of fuel costs through the Fuel Adjustment Clause ("FAC"). Approximately \$12.2 million of the \$14.5 million payment is Kentucky jurisdictional.

The intervenors in this case were the Utility and Rate Intervention Division of the Kentucky Attorney General's Office ("AG") and the Kentucky Industrial Utility Customers ("KIUC"). A public hearing was held on August 3, 1988.

KU negotiated the early release from its Coal Ridge contract which was not scheduled to terminate until December 31, 1991. In executing the release, KU paid Coal Ridge \$14.5 million and entered into a 12-month fixed price contract for delivery of 24,000 tons per month beginning in April 1988.

The evidence presented by KU showed that by terminating the Coal Ridge contract its customers will receive the benefits of lower current coal prices and anticipated lower future coal prices. KU estimated that the total fuel cost savings of the coal contract release is approximately \$27.4 million, for a net savings in fuel expense of approximately \$12.9 million after deducting the initial prepayment of \$14.5 million. The present value of the net savings was estimated to be \$10.4 million.

KU proposed to account for the release by establishing a deferred debit of \$14.5 million in Account 186, Deferred Debits. KU then would charge the buy-out cost, amortized over the 44 months remaining life of the contract, to Account 151, Fuel Stock, for inclusion in the monthly FAC calculation. KU stated that its customers will receive the benefits of reduced fuel costs throughout the remaining life of the contract, therefore, recovery of the buy-out costs over that same period is proper and equitable.

Neither the AG nor KIUC opposed KU's buy-out of the Coal Ridge contract and neither intervenor objected to KU's proposed accounting treatment for the recovery of the \$14.5 million. However, both the AG and KIUC argued that this case should be held in abeyance until Case 9631, An Investigation Into The Fuel Procurement Practices Of Kentucky Utilities Company, is completed. The intervenors argued that a decision in this case is dependent upon the Commission's final ruling in Case No. 9631 on the prudence of the original contract. However, as an alternative,

the intervenors suggested that approval of KU's request be granted on an interim basis subject to refund pending the final outcome of Case No. 9631.

KU contended that the issues in this case are essentially identical to the issues in Case No. 8921, Application Of Big Rivers Electric Corporation For An Order Approving Certain Accounting Treatment Of Amounts Paid For Coal Contract Amendment, in which the Commission approved recovery of a prepayment through the FAC. KU also argued that an Order approving recovery in this case need not be subject to refund, so long as the Order is without prejudice to the investigation pending in Case No. 9631.

The Commission finds the issues in this case to be quite similar to the issues in Case No. 8921, but not identical. This case represents a buy-out of a contract, whereas Case No. 8921 involved a "buy-down" to reduce future prices. The Big Rivers' contract amendment secured a long-term source of coal from the existing supplier, while the buy-out in this instance puts KU in the market to purchase coal from several potential suppliers.

Despite these differences, there are significant similarities and reasons for approving KU's proposed accounting treatment and recovery through the FAC. The \$14.5 million represents a prepayment of fuel costs for the purpose of obtaining a current and future reduction in fuel expense; the buy-out results in an immediate benefit to KU's customers which will continue through the remaining life of the contract; and denial of

the proposed recovery would tend to discourage utilities from attempting to negotiate for lower rates and prices in existing contracts. The Commission, therefore, is of the opinion that KU's proposal should be approved.

In approving recovery of costs associated with this particular contract buy-out, the Commission is not establishing a precedent whereby these type costs can automatically be passed through the FAC. Contract buy-outs (and buy-downs) differ in terms and circumstances. Such costs can be determined as appropriate for FAC recovery only after review of a formal application.

The Commission is not persuaded, however, by KU's argument that approval and recovery should not be subject to refund. We intend to insure that KU's customers' rights and interests remain fully protected pending the outcome of Case No. 9631. Therefore, the jurisdictional amounts recovered by KU through the FAC for the amortization of the lump sum payment to Coal Ridge should be collected subject to refund.

FINDINGS AND ORDERS

The Commission having considered the evidence of record, is of the opinion and finds that:

1. The \$14.5 million, approximately \$12.2 million Kentucky jurisdiction, paid by KU is in effect a prepayment of fuel costs to obtain current and future coal market price benefits for its customers, and, therefore, the FAC regulation, 807 KAR 5:056, provides for the recovery of such a prepayment.

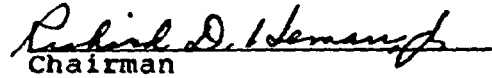
2. KU should amortize the prepayment over a period of 44 months for recovery through the FAC beginning in October 1988 and continuing through May 1992.

3. The amounts collected by KU through the FAC for the amortization of the jurisdictional portion of the \$14.5 million prepayment are subject to refund pending the outcome of Case No. 9631.

The above findings are HEREBY ORDERED.

Done at Frankfort, Kentucky, this 7th day of October, 1988.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director